

United States Senate
Committee on Finance



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Prepared Remarks of Sen. Chuck Grassley
On Charities and Governance
Buchanan Ingersoll & Rooney, Washington, D.C.
Tuesday, March 10, 2009

Good morning. I want to thank Buchanan Ingersoll & Rooney for hosting me here today, particularly Chairman Thomas and Bob Winters who I understand is the one who made this happen. Chairman Thomas and I worked closely together to enact significant legislation impacting charities, including the JOBS bill, Tax Increase Prevention and Reconciliation Act, and most importantly, the Pension Protection Act of 2006. Aside from legislating, Chairman Thomas and I conducted oversight of certain types of charities. While I am sure there were others, the two that I remember we shared a joint interest in were college athletics and tax-exempt hospitals. I think it's fair to say that we believe in strengthening the charitable sector by making charities more accountable for the significant tax breaks bestowed on them in the tax code. So I am pleased to be here with him and all of you today to discuss my work in this area so far and talk about some of things that continue to concern me.

Over a hundred years ago, Alexis de Tocqueville wrote about the unprecedented influence of the nonprofit sector here in the United States. And I believe that the strength of the sector remains unrivaled in the world even now. The generosity of private donors, whether they are an individual, a corporation or charitable foundation, is also beyond comparison. This generosity, and the belief that these donors can act more efficiently and effectively than government, is what makes the independent sector here the envy of other nations. Just as we are known the world over for our generosity and the strength of the charitable sector, we are also known for expecting – and demanding – accountability, especially when it comes to government intervention and expenditures.

I am probably best known among this group for my oversight of the IRS and charitable organizations. But, throughout my career, I have conducted extensive oversight of other government agencies and programs including the Departments of Health and Human Services, Defense and Justice, the Food and Drug Administration, Federal Bureau of Investigations and the Securities and Exchange Commission. I view it as my constitutional duty to conduct oversight, regardless of who is in the White House or which party controls Congress. As a legislator, I work to improve accountability in two ways. The first obviously is to legislate but

the other is to conduct oversight through hearings and investigations. When it comes to charities, I have done both, but there is a lot left to do.

As Chairman of the Finance Committee, I started looking into charities and the tax laws that govern them because I was concerned about the abuse of charities and charitable deductions. I have learned much as a result. I learned that charities like supporting organizations and donor advised funds were raking in a lot of money and engaging in self-dealing transactions. But they weren't subject to the same rules as private foundations. I learned that certain charities like credit counseling organizations, hospitals, student loan organizations or veterans charities were acting no differently from for-profit, commercial entities. In some cases, they existed solely for the benefit of their founders. I learned that the boards of tax-exempt organizations like the Red Cross, The Nature Conservancy, American University and The Smithsonian were not engaged in setting strategic direction for the organization or were not actively monitoring conflicts of interest or excessive compensation. I learned that charities desperate for sources of revenue would facilitate tax shelter transactions or the abuse of charitable contribution deductions such as vehicle donations. While the different legislation I mentioned earlier stopped many of these abuses, charities themselves also implemented reforms on their own. I have asked many questions and asked my staff to put out proposals for reform for discussion. As a result, there has been unprecedented dialogue between the charitable sector and Congress. I personally have appreciated the work of the Panel on the Nonprofit Sector, spearheaded by Diana Aviv and Sister Carol Keehan at the Catholic Health Association. Both of these women avoided the chicken-little approach and engaged me in intelligent, thoughtful conversation about reforms. The reports from the Panel on the Nonprofit Sector guided Congress in determining what issues needed further attention before legislating. Similarly, Sister Carol's input regarding hospital legislation convinced me to ask my staff to rework the legislative proposal on charitable hospitals.

Charities are an integral part of American society. They often step in to fill the void by providing services that the government or the private sector does not provide. They are on the front lines every day, in good times and in bad. They feed the hungry, shelter the homeless and provide care for the most vulnerable in our society. While touring the flood-ravaged areas in Iowa last summer, I saw firsthand how important local charities and volunteers were to the response and recovery efforts. It reminded me that those closest to a problem are frequently those who know best how to respond. We also saw this in the response to Katrina. The churches and other community organizations there were able to provide food and shelter more quickly than FEMA or the Red Cross. They probably could have done even more if they had the capacity or there was a system in place for them to be accountable for taxpayer and government money.

The federal government acknowledges the important role that charities play in American society by supporting the development and growth of this sector in many ways. The most notable are the tax subsidies found in the tax code, including income tax-exemption for certain organizations, deductions for contributions to charities, and tax-exemption for interest on bonds issued by them. In addition, agencies, such as Health and Human Services and Housing and Urban Development, not only partner with charitable organizations but also provide direct financial assistance to them. We also have the Corporation for National and Community Service which promotes community service through programs such as AmeriCorps and Senior Corps.

This significant federal government support of the sector is what drives me to continue asking questions and to consider legislation.

This year marks the 40th anniversary of the enactment of the 1969 private foundation rules. In these 40 years, we have seen explosive growth in charities and charitable giving. What we haven't seen, though, is the law, and the enforcement of the law, keep up with that growth. In the 1960s, Congress was concerned that private foundations were not paying out enough. Congress was also concerned that donors to them were using them for their own benefit or to fund questionable investments, including family businesses.

However, since the 1969 Act passed, we have seen an explosion in other types of grant-making vehicles like supporting organizations, donor-advised funds, endowment funds, and more recently, venture philanthropy funds. Since some of these walk and talk like private foundations, it's fair to ask why the private foundation rules shouldn't apply to them. For example, some are struggling because of poor investment decisions. Harvard's investment in illiquid private equity and hedge funds means they have to take out a loan or issue bonds to increase liquidity. Those who invested with Madoff appear to have boards that may have looked the other way in return for the promise of high earnings.

Both of these examples raise the question of why the jeopardy investment excise tax should only apply to private foundations. On the other hand, some of the rules create perverse incentives for private foundations to give out more money. For example, a large foundation that decides it wants to continually fund a small charity may actually "tip" that charity into private foundation status. Or, if it increases its payout, it may be subject to an increased excise tax on its investment income a few years down the road. And for those foundations that view the 5 percent threshold as a floor rather than a ceiling, there is no reward. They get treated the same as those who treat the 5 percent as a ceiling and don't pay out any more. It would seem that these are unintended consequences of the 1969 rules. Discussing changes to these rules is timely since many charities are struggling with liquidity during this economic crisis.

In contrast to Harvard's endowment fund or those who invested with Madoff, many charities are struggling with liquidity for other reasons. Credit lines are no longer accessible, charitable donations and grants have decreased, or the state and local governments with which they have contracts have not paid up. Congress was asked to consider some proposals in the stimulus bill. But I wasn't convinced they were the best solutions or would actually help charities. The federal bridge loan fund proposal -- to help small charities that are not being paid timely on their contracts with state and local governments -- is worthy of consideration. However, it begs the question of why various grant-making entities and funds couldn't pool their resources to do the same thing or just increase their payouts. Maybe we should work toward a law that mandates that states have to be timely in their payments. I filed an amendment to the stimulus bill that required states to be current on their payments before accepting any federal money from the F-MAP slush fund. Since all Republican amendments were being voted down, I didn't see the point in offering it. Contract fulfillment is not technically not in the Finance Committee's jurisdiction, but I'd like to find a way to help charities get the money they have been promised.

As I just stated a few minutes ago, the proposal to simplify the private foundation excise tax is also worthy of consideration but not necessarily as stimulus. Some foundations have decided it's the right thing to do to increase payout now and worry about the additional excise tax later. That makes me wonder whether foundations that are lobbying for this rule change would actually increase their giving if Congress were to enact it today.

There is also a proposal to loosen private rules and regulations to allow them to more easily fund certain for-profit entities. There is very little information about these new entities, known as low-profit, limited liability companies, or L3Cs. Neither the Finance Committee nor the Ways and Means Committee has conducted any hearings about them. So I was a little surprised that the loosening of the tax rules for them was proposed as a stimulus initiative. It's too early for us to consider this proposal

Finally, the proposal to expand the IRA rollover provision to increase the amount and allow individuals to roll over into donor-advised funds seemed more about assisting individuals reduce their tax liability than assisting charities on the front lines. If we are trying to get more money out to the charities and people in need, it's hard to see how rolling over money into a fund with no payout requirement gets money to where it can help the most.

The question of the effectiveness and efficiency of the tax breaks for giving to charity is an important one. The President's budget proposal to limit the deductibility of charitable contributions for so-called wealthy individuals is shining a spotlight on this issue. Some argue that such a limitation would not impact charitable giving. Others argue that it would. There is agreement that the proposal is complex. I question the wisdom of providing any disincentives for giving during this economic crisis. I'm sure we will all hear about this more as the Finance Committee explores this and other budget proposals. At this point, it is not clear what, if any, legislation regarding charities or charitable deductions will be enacted in this Congress. However, as I mentioned earlier, legislation is only one tool in improving accountability.

In conducting oversight, I believe that sunshine is the best disinfectant. The more information that is available to the public and to Congress, the better. So, I will continue to work with Chairman Baucus to conduct hearings and I will continue to write to specific charities to better understand their activities. I also expect my staff to continue drafting legislative proposals and conduct roundtable conversations.

Finally, I will continue to press the Internal Revenue Service to improve reporting requirements for charities, particularly for private foundations and colleges and universities and to improve its enforcement efforts, including its compliance studies. Improving the accountability of charities through increased transparency, whether through hearings, investigations or reporting requirements, will instill greater confidence in the donors who fund and support them. We must ensure that our long and successful tradition of philanthropy remains the envy of the world. This has been the heart of my efforts over the last seven years and it is what I will continue to push for. Thank you for your attention and I'd be happy to take questions.

